Actuarial Expectations -- Executive Director Update
November 19, 2012

Members' Responses

ATRS is expected to need approximately 2.75% of payroll to bring its unfunded liabilities to 30 years. In anticipation of actuarial results, the ATRS staff has researched several cost cutting measures that would reduce the unfunded liabilities while still maintaining the **3 R's** of ATRS' contribution to education: **Recruitment, Retention**, and **Rewarding**. The staff stands ready to work with the Board to develop any of these measures or any other changes to better stabilize the funding status of the System.

It should be noted that the ATRS investment portfolio has grown from about $11.4 billion dollars to $11.7 billion dollars since July 1, 2012. If the return on investments continues to grow, the cost cutting measures **may not be necessary at all**, or may be rolled back if the portfolio rises sufficiently between now and June 30, 2013. Because ATRS assumes an 8% return on investments, the return must be greater than 8% to begin paying off the unfunded liabilities. Each 3% of return rate above 8% is equivalent to about a 1% employer contribution rate increase. If the return rate for the year ended June 30, 2013, were to be 18% or greater, then ATRS should be in great shape. If the return is not enough, then some of the following cost cutting measures may be necessary.

The ability to reduce the unfunded liabilities of ATRS can begin with some simple concepts. There are limited ways to reduce the liabilities. In the simplest of terms, ATRS can **increase revenue**, pay out less **now**, or pay out less **in the future**. It begins at that simple level. As the ATRS Board studies how to reduce the unfunded liabilities of ATRS, the areas to reduce the liabilities can be put into 3 categories:

1. **Increase revenues.** This can be done two ways, either by having investment returns of more than 8% or by increasing the contribution rate for employers or members.

   I vote no for increases in the contribution rate for both employees and employers.

2. **Decrease current payouts.** This can be done by reducing the retirement benefits being paid to current retirees.

   Please do not adjust the current payout to retired members. It is inherently unfair for those of us in retirement to bare this burden. I hope you and the ATRS Board will not consider cutting the benefits or changing the retirement age/years of service requirements. Those who have already retired and

those who are nearing retirement have planned and sacrificed to finally enjoy the benefit of retirement. It would be unfair to change the rules in the later years of the teacher's careers. Radical changes could even deter new teachers from the profession. We don't need quality teachers driven away.

I vote no for decreases in the current payouts.

A member who has 35 years of service and is in the fourth year of T-DROP is also concerned about benefits changing. Mr. Hopkins replied the only changes that could affect a member in T-DROP are the ones that reduce or eliminate the $75 per month stipend additive paid to any member with more than ten years of service. If any stipend changes are implemented as presented, that amount will not be payable to you and any portion of your monthly T-DROP accrual, based on the elimination/reduction of the stipend will also not be deposited. Plus, once you actually retire, the amount that the stipend is cut will not be paid to you monthly.

As a retiree, I am very much against lowering the benefits of those already drawing checks. It would be unfair for the retirement system to take back the promise made to me and other retirees. One problem with the system is the influx of retired teachers from other states that can enter our system and draw benefits after only five years in Arkansas. In our area, many have been superintendents who draw high salaries for their three years of benefit calculation. Please do not penalize the former classroom teachers who worked for so many years and draw such a minimal amount that we must supplement our income with extra work just to survive this economy!

3. **Slow the accrual of future benefits.** This can be done by lowering the benefits that will be paid to current T-DROP and active members. Examples are: lower the multipliers, lower T-DROP interest rates, lower survivor benefits, raise age to get unreduced benefits, use a 4 or 5 year final average salary, and other benefit cuts.

   I think averaging using the last 3-4 years is a great idea. I also strongly support requiring 26 years instead of the current 25, being used as a first year for retirement (if not attained 60) and tweaking of T-DROP.

There should be no interest or earnings benefits paid on T-DROP accounts left with ATRS that are above the earnings that could be realized in secured fixed income accounts in the private sector. NO benefits from the Systems' stock investments without the risk.

I vote yes for slowing the accrual of future benefits.

Cost Cutting Measures Being Studied by the ATRS Board

A. Increase Employer Contribution Rate by 1%. ATRS could ask for an employer contribution rate increase. This proposed legislation could be drafted in such a way that the Board could scale the contribution rate back to a lower amount as the unfunded liabilities diminish. The benefit of this proposal would be **1.00%, 0.75%, or 0.50%** of payroll, or equivalent to a 1.00%, 0.75%, or 0.50% increase in the employer contribution rate**.** This proposal would affect all employers, including some state agencies and colleges. If the ATRS Board seeks an increase in the employer rate, the amount requested would be an ATRS Board decision. The General Assembly would be required to approve the increase before it could occur.

I vote no for increases in the contribution rate for both employees and employers.

B. Contract Buy Out, Settlement Agreements, Court Ordered Payments, Contract Won Through Litigation, Judgment or Decree. Staff Recommendation to Replace All Other Approved or Discussed Proposals. The ATRS staff is proposing that ATRS consider any salary that is reported under the IRS guidelines of W2 income that is reported to ATRS within 30 days of an accepted contract buy-out, settlement agreement, final court ordered payment, contract won through litigation, judgment, or decree will be treated as salary for the purpose of paying ATRS benefits. If the member is contributory, the mandatory 6% withholding must be reported on the salary. The employer contribution must be paid on the reported salary. Service credit shall be for the time actually worked. This salary shall not be stacked with W2 salary earned while working the normal duties of the job requirements. ATRS will accept the higher of the two amounts in the final average salary if one should be considered as one of the highest of the final average salaries. Any W2 salary reported after the 30-day cut-off period shall not be treated as salary for benefit purposes, but will require employer contributions. Any "air time" that a member should have been eligible to work as a result of a wrongful termination may be purchased at the actuarial cost of service for the time the service would otherwise have been earned.

C. **1% Reduction for Noncontributory Service in T-DROP Formula.** The ATRS Board has recommended legislation that would require a 1% reduction for each year of noncontributory salary used in the T-DROP reduction formula. This would make all service credit types have the same reduction: contributory, noncontributory, and reciprocal. The cost savings for this proposed legislation is **.08%** as a percent of payroll, equivalent to a .08% increase in the employer contribution rate, which would be recognized immediately by the actuaries.

I have been in the T-DROP program for the past 18 months and from reading all the information provided in the newsletter, it seems my projected retirement might be lowered? Mr. Hopkins replied that when already in T-DROP, all retirement calculations are set.

Another member who has 35 years of service and is in the fourth year of T-DROP is also concerned about benefits changing. Mr. Hopkins replied the only changes that could affect a member in T-DROP are the ones that reduce or eliminate the $75 per month stipend additive paid to any member with more than ten years of service. If any stipend changes are implemented as presented, that amount will not be payable to you and any portion of your monthly T-DROP accrual, based on the elimination/reduction of the stipend will also not be deposited. Plus, once you actually retire, the amount that the stipend is cut will not be paid to you monthly.

D. **Four Year Final Average Salary Immediately.** The ATRS Board has the authority in the existing law to set the applicable number of years to be used in computing final average salary through the promulgation of rules. ATRS has been using the highest three years to calculate final average salary since April 1, 1998. By increasing the years in the formula to four, the immediate cost cutting savings would be **.39%** as a percent of payroll, equivalent to a .39% increase in the employer contribution rate.

I think averaging using the last 3-4 years is a great idea. I also strongly support requiring 26 years instead of the current 25, being used as a first year for retirement (if not attained 60) and tweaking of T-DROP.

E. **Four Year Final Average Salary in 2019.** ATRS staff has evaluated the effect of changing the years in the final average salary on July 1, 2013. The staff believes this could bring about a change in member behavior as members rush to retire in order to take advantage of the three year final average salary. This could leave classrooms empty, cause a disruption in education, and bring about a drain on the trust fund assets. If the final average salary years increase were to be pushed six years into the future, with a provision that **if** the unfunded liabilities of the System drops to 30 or less years, then the final average salary would remain unchanged at three years, then ATRS can have cost savings without harm to ATRS or the quality of education. The cost savings of this proposal would be **.26%** of payroll, equivalent to a .26% increase in the employer contribution rate**.** This proposal would give the fund adequate time to build assets before the need for an actual implementation, allow the Board to withdraw it if it is not needed, reduce the risk of a rush to retire, and still give the Board the flexibility to effect cost cutting measures as needed.

I think averaging using the last 3-4 years is a great idea. I also strongly support requiring 26 years instead of the current 25, being used as a first year for retirement (if not attained 60) and tweaking of T-DROP.

F. **Five Year Final Average Salary Immediately.** As stated in the paragraph above, the ATRS Board has the authority in the existing law to set the applicable number of years to be used in computing final average salary through the promulgation of rules. ATRS has been using the highest three years to calculate final average salary since April 1, 1998. By increasing the years in the formula to five, the immediate cost cutting savings would be **.76%** as a percent of payroll, equivalent to a .76% increase in the employer contribution rate.

G. **Five Year Final Average Salary in 2019.** ATRS staff has evaluated the effect of changing the years in the final average salary on July 1, 2013. The staff believes this could bring about a change in member behavior as member rush to retire in order to take advantage of the three year final average salary. This could leave classrooms empty, cause a disruption in education, and bring about a drain on the trust fund assets. If the final average salary years increase were to be pushed six years into the future, with a provision that if the unfunded liabilities of the System drops to 30 or less years, then the final average salary would remain unchanged at three years, then ATRS can have cost saving without harm to ATRS or the quality of education. The cost saving of this proposal would be **.50%** of payroll, equivalent to a .50% increase in the employer contribution rate. This proposal would give the fund adequate time to build assets before the need for an actual implementation, allow the Board to withdraw it if it is not needed, reduce the risk of a rush to retire, and still give the Board the flexibility to effect cost cutting measures as needed.

H. **Eliminate $75 Stipend Flash Cut.** Currently most ATRS retirees receive a $75 dollar per month benefit supplement called the "**stipend**". The stipend can be eliminated or reduced by legislation. Reducing the income of retirees would be a difficult undertaking. ATRS realizes many retirees are dependent on the added amount of $75 dollars from the stipend each month. The stipend was added to retirees' benefits on July 1, 1999. The original amount of the stipend was $50 per month, and was added to every retiree, survivor, and beneficiary regardless of the amount of service credit. The following year, the stipend was increased to $75 per month, again with no requirements for eligibility. Beginning with retirees on or after July 1, 2001, the eligibility requirement was raised to five years of service credit, and beginning July 1, 2007, the eligibility requirement was raised to ten years of service credit. As the number of retirements has grown, so has the cost of the stipend. The cost savings of a flash cut to end the stipend would be **1.51%** of payroll, equivalent to a 1.51% increase in the employer contribution rate.

My personal preference is eliminating the $75 for retirees.

DO NOT eliminate the $75 stipend for retirees. Some just get by financially with this $75 per month.

We have no objection to rolling back stipends if that is not the only cost-cutting measure used to bring actuary to 30-year requirement.

I. **Reduce Stipend to $50.** The ATRS staff has also had a study performed to reduce the stipend by only $25 per month beginning July 1, 2013. Again, this is not a recommendation, but one of many options the staff feels it has a duty to report to the Operations Committee and Board. This cost savings of this proposal would be **.47%** of payroll, equivalent to a .47% increase in the employer contribution rate.

DO NOT eliminate the $75 stipend for retirees. Some just get by financially with this $75 per month.

J. **Eliminate $75 Stipend over Three Years.** If the stipend were to be reduced by $25 each month for each of three fiscal years beginning July 1, 2013, the cost savings would be **1.39%** of payroll, equivalent to a 1.39% increase in the employer contribution rate. The stipend would be cut to first $50 dollars per month the first year, $25 dollars per month the second year, and would disappear in the third year.

DO NOT eliminate the $75 stipend for retirees. Some just get by financially with this $75 per month.

K. **Increase Member Contribution Rate by 1%.** The ATRS member contribution rate has been 6% of salary for contributory members for 43 years, including the current 2012-2013 year. Many states have increased member contribution rates in recent years. Again, this is intended to give the Operations Committee and Board full disclosure of possible funding measures. By increasing the contributory member contribution rate from 6% to 7%, ATRS would recognize an annual revenue increase in trust fund revenue equal to approximately **.70%** of payroll, equivalent to a .70% increase in the employer contribution rate.

   If any changes are needed, consider raising the teacher contribution to 7% and the school contribution to 15%.

   I vote no for increases in the contribution rate for both employees and employers.

L. **Increase Member Contribution Rate by 2%.** If the ATRS contributory contribution rate were increased from 6% to 8%, ATRS would recognize an annual revenue increase in trust fund revenue equal to approximately **1.40%** of payroll, equivalent to a .1.40% increase in the employer contribution rate.

   If any changes are needed, consider raising the teacher contribution to 7% and the school contribution to 15%.

   I vote no for increases in the contribution rate for both employees and employers.

M. **Change Contributory Multiplier for Future Service to 2.10%.** As staff began to look at cost cutting measures, each segment of membership was evaluated to see if the cost could be shared among the various groups. If the contributory multiplier were reduced from the current 2.15% to 2.10% on contributory service credit earned after July 1, 2012, (all previously earned service credit would remain at the 2.15% multiplier) the cost savings would be **.24%** of payroll, or equivalent to a .24% increase in the employer contribution rate. **For emphasis,** all previous years worked as a contributory member would remain at the current 2.15% multiplier.

Consideration should be given to some reduction in the multiplier for future years of contributory service coupled with a gradual increase in the 30 years of service. As life expectancy has increased, the years required for full retirement benefits have not. Also, consideration should be given to reducing the multiplier for years above 30 and to reducing the contribution amount to the T-DROP accounts as well.

N. **Change Noncontributory Multiplier for Future Service to .75%.** As the contributory multiplier in the benefit formula was evaluated, so was the noncontributory service credit multiplier. Staff gave two suggestions for reductions to the formula for noncontributory service credit earned after July 1, 2013. All previous years worked as a noncontributory member would remain at the current 1.39% multiplier. The first proposal would reduce the current 1.39% multiplier to .a 75% multiplier for all noncontributory service credit years worked after July 1, 2013. This cost saving would be .**78%** of payroll, equivalent to a .78% increase in the employer contribution rate. One difference here is that a noncontributory member can avoid a reduction by signing a simple one page form to become contributory and get the much higher contributory multiplier.

   Reduce noncontributory multiplier.

   The only request I personally have is that I, as a noncontributory member, be allowed to change to contributory. (Mr. Hopkins let this member know that they can fill out a form to request to become contributory and if done now, it will be effective July 1, 2013.)

O. **Change Noncontributory Multiplier for Future Service to .6%.** The second noncontributory multiplier proposed for a cost study would reduce the current 1.39% multiplier to .6% on all noncontributory service credit earned after July 1, 2012. All previous years worked as a noncontributory member would remain at the current 1.39% multiplier. Although the reduction appears to be harsh, this is one area that the individual noncontributory members can remedy. By signing a one page form to change to contributory status at the beginning of a fiscal year, then these members would not be impacted if this proposal were to be adopted. The cost savings for this proposal would be .**91%** of payroll, equivalent to a .91% increase in the employer contribution rate.

   Reduce noncontributory multiplier.

P. 10 Year Vesting. The staff obtained a cost study to evaluate the cost savings if ATRS returned to ten year vesting on future retirees. The proposal assumes that any member who is not vested (less than five actual years of service credit) as of July 1, 2013, and new hires would have to have 10 years of service credit for full voluntary retirement at age 60, for deferred retirement at age 60, and for disability and survivor benefit eligibility. The cost savings for this proposal would be **.16%** of payroll, equivalent to a .16% increase in the employer contribution rate**.** For the small amount of savings, the staff foresees many problems with disability retirement, survivor rights, and reciprocal service credit with other Arkansas public retirement systems that would not justify this proposal due to the relatively small cost savings.

Retirement was vested at ten years and then reduced to five. Going back to ten while allowing a one year window for those with immediate plans only makes sense. Anything that allows reciprocal service to gain an immediate benefit through system switching should be immediately eliminated as well.

Q. Discounted Purchase of Benefit Rights for Inactive Vested Members. Currently, the ATRS liabilities in total include liabilities of about $700 million dollars to members who are, or will become inactive vested members. This means that over 4% of the ATRS liabilities are to members who are no longer on a career path and are no longer involved in delivering the educational curriculum to Arkansas schools.

Many of these members also wish to cancel their service and obtain an immediate payment versus being entitled to receive a monthly retirement benefit that may not occur for 20 or more years into the future. Members who are totally contributory have somewhat of an option now, and that is to obtain their contributions plus interest. The members with mixed service of contributory and noncontributory can do the same. The members that are totally noncontributory have no method of cashing out their service for immediate payment. The Board has recommended this proposed legislation to allow these members to exchange their right to a benefit in the future for an immediate cash payment now to take these liabilities off the ATRS books at a discount.

This would affect over 12,000 inactive vested members if the member choses to take a settlement payment. This proposal would require Board action from time-to-time to open a window for these discounted liquidations. This program would be totally voluntary, and would be a cost saving of **.42%** of payroll, equivalent to a .42% increase in the employer contribution rate.

The suggestion that allows the members draining some of the funds should be allowed to get their money. If we are keeping them until 60 to get benefits, and they have left education, why are we abusing our system for non-educators?

R. **Refund Contributions after Five Years of Inactivity.** This proposal was a law in the early years of Arkansas Teacher Retirement. Members who were required to cash out were often disadvantaged if they return to covered employment, due to the cost of repaying refunds. With the actuarial cost service in effect now, very few members would ever be financially able to restore the service credit. However, this was another segment of members that ATRS staff considered when evaluating the various populations of membership data. This cost savings for this proposal would be approximately **.24%** of payroll, equivalent to a .24% increase in the employer contribution rate.

S. **Tier 2 Low Cost.** ATRS staff proposed two different tier plans for cost studies by the actuaries. The least costly plan would require 30 years of service credit for full voluntary retirement, no stipend would be provided, the cost of living adjustment would be set by the Board with a range of 0% to 2.5%, and the noncontributory multiplier would be set at .7%. The ATRS staff is hesitant to establish another tier of benefits due to the overhead of administration. Even if the tier could be rolled back into the regular retirement plan at some future date, there would be some retirees in the tier plan for many years due to the combination of ATRS service credit with reciprocal service credit from other Arkansas public retirement systems. The cost savings of this tier would be approximately **.60%** of payroll over time, equivalent to a .60% increase in the employer contribution rate.

T. **Tier 2 High Cost.** ATRS staff developed this tier with as many cost reductions as possible. The provisions of this tier included 35 years of service credit requirement for full voluntary retirement, vesting at 10 years of service, age based retirement would increase from 60 to 65 (less than 35 years of service credit), no stipend, 0% to 2.5% cost of living adjustment to be set by the Board, 10 years of service credit requirement for survivor or disability retirement, a six month separation period for all retirees, regardless of service credit or age, no death benefit, and a noncontributory multiplier of .7%. The actuaries estimated a cost savings of approximately **1.07%** of payroll over time, equivalent to a 1.07% increase in the employer contribution rate.

Tweaking the system for those who have 10 or fewer years in ATRS are the most fair and have the greatest potential impact on the long term health and viability of the system. Those are the

folks who have the time needed to make necessary adjustment in order to prepare. For us, there is NO TIME, for many of us depend solely on the benefits and have no other options. Please protect us and let the rest of the burden be shared across the system, but mostly on the front end of the process (those entering and in their very first years).

The "pain" of cost cutting should be born equally by retirees, active members and employers.

<u>Other</u>

NO retiree should be able to retire and go back to the same job unless they are low compensated employees. I am a retired superintendent and still work but only part time and in a different job and after at least six months' separation. All members retiring and continuing to work should do so under similar circumstances. NO same job/same employer. NO pre-arrangements of any kind.

Go back to 30 years of service for non-reduced retirement.

I agree that if ATRS doesn't make some adjustments/decisions, it has made the decision that someone else will make decisions for ATRS.

After reading the documents, we feel ATRS has looked thoroughly for waste and "padding" of our funds. Thank you for beginning this much needed process.

I suggest that ATRS allow retirees to work at colleges without any separation at the time of retirement since most colleges only have grandfathered members of ATRS still working there.

One problem with the system is the influx of retired teachers from other states that can enter our system and draw benefits after only five years in Arkansas. In our area, many have been superintendents who draw high salaries for their three years of benefit calculation.